UNITED STATES DISTRICT COURT

DISTRICT OF MAINE

MARCEL R. MORIN, et al.,	***)***	
	)	
Plaintiffs	***)***	
	)	
v.	***)***	***Docket No. 96-381-P-H***
	)	
T.P.M., INC., et al.,	***)***	
	)	
Defendants	***)***	

RECOMMENDED DECISION ON DEFENDANTS' MOTIONS TO DISMISS AND FOR JUDGMENT ON THE PLEADINGS AND MEMORANDUM DECISION ON PLAINTIFFS' MOTIONS TO AMEND THE COMPLAINT

This action arises out of the sale of the assets of a limited partnership, Tall Pines Manor Associates. The plaintiffs own eight shares of a total of thirty in the limited partnership. Defendant Health Care Management, Inc. ("HCM") has filed a motion to dismiss the action, and the other defendants, with the exception of PropSys, have filed a motion for judgment on the pleadings. The plaintiffs have responded, in part, with two motions to amend the complaint, to dismiss one defendant, and to add one defendant. I grant the motions to amend and recommend that the court grant in part the motions to dismiss and for judgment on the pleadings.

I. The Motions to Amend

The plaintiffs' first motion to amend their complaint (Docket No. 15), filed on April 14, 1997, seeks to dismiss Tall Pines Manor Associates as a defendant, add Larry M. Brown as a

defendant, to restyle the complaint as a partnership derivative action, to drop a claim under 15 U.S.C. § 77q (Count I in the initial complaint), to replead a negligence claim as one for negligent misrepresentation, to expand the factual allegations included in a claim under the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1961 *et seq.*, to add counts alleging diversion of a business opportunity and conspiracy under state law, and to refine several other factual allegations, including clarification as to which counts are asserted against which of the seven defendants. The plaintiffs' second motion to amend their complaint (Docket No. 18), filed April 25, 1997, seeks to add several factual allegations to the existing counts and rewrite the RICO claim (Count XI). Defendant HCM filed an objection to the first motion (Docket No. 21), and all defendants have objected to the second motion (Docket Nos. 22 and 23). No scheduling order has yet been entered in this action.

Fed. R. Civ. P. 15(a) provides that leave to amend a pleading shall be freely given when justice so requires. It is this court's practice to include in its scheduling order a deadline for the joinder of additional parties and amendment of the pleadings. Local Rule 16.2(c). Here, the plaintiffs have sought leave to add a defendant, drop a defendant, and amend their complaint before a deadline for such activity has even been established by the court. HCM opposes the first motion to amend, without citation to any authority, on the grounds that the proposed amendments fail to change the grounds for its assertion in its motion to dismiss that the complaint fails to state a claim upon which relief may be granted against HCM. Its objection to the plaintiffs' second motion to amend makes the same unsupported argument. The other defendants object to the second motion on the grounds that their pending motion for judgment should be decided before the proposed amendments are addressed and that the amended complaint fails to state a claim on which relief may

be granted as to the proposed derivative action.

Because none of the defendants has objected to the dismissal of Tall Pines Manor Associates as a defendant and the addition of Larry M. Brown as a defendant, those portions of the initial motion to amend will, of course, be granted. The motions to amend are timely, there is no suggestion of bad faith, and the proposed amendments are not prejudicial to the defendants. *Foman v. Davis*, 371 U.S. 178, 182 (1962); *Tiernan v. Barresi*, 944 F. Supp. 35, 38 (D. Me. 1996). A party against whom a motion to dismiss under Rule 12(b)(6) is filed ordinarily is given an opportunity to amend the complaint before the motion is ruled upon. *Neitzke v. Williams*, 490 U.S. 319, 329 (1989); *Wyatt v. City of Boston*, 35 F.3d 13, 14 (1st Cir. 1994). The substance of the proposed additions to the complaint can best be addressed, as the defendants have done in their memoranda of law, in the context of the pending motions to dismiss and for judgment on the pleadings. Therefore, the motions to amend are granted in their entirety.

II. The Defendants' Motions

A. Standard for Reviewing Motions

"When evaluating a motion to dismiss under Rule 12(b)(6), [the court] take[s] the well-pleaded facts as they appear in the complaint, extending the plaintiff every reasonable inference in his favor." *Pihl v. Massachusetts Dep't of Educ.*, 9 F.3d 184, 187 (1st Cir. 1993). The defendant is entitled to dismissal for failure to state a claim "only if it clearly appears, according to the facts alleged, that the plaintiff cannot recover on any viable theory." *Correa-Martinez v. Arrillaga-Belendez*, 903 F.2d 49, 52 (1st Cir. 1990); *see also Jackson v. Faber*, 834 F. Supp. 471, 473 (D. Me. 1993). Review is limited to allegations in the complaint; the court may not consider factual

allegations, arguments, and claims that are not included in the complaint. *Doyle v. Hasbro, Inc.*, 103 F.3d 186, 190 (1st Cir. 1996). The court applies the same standard to a motion for judgment on the pleadings. 5A C. Wright & A. Miller, *Federal Practice & Procedure* § 1367 at 515 (2d ed. 1990); *see also Slotnick v. Garfinkle*, 632 F.2d 163, 165 (1st Cir. 1980).

B. Factual Background

The second amended complaint makes the following relevant factual allegations. The plaintiffs, four individuals and four couples, are limited partners of Tall Pines Manor Associates ("Tall Pines"), a Maine limited partnership. Amended Complaint ¶¶ 1-2. Defendant T.P.M., Inc. ("TPM") is a Maine corporation that is the managing general partner of Tall Pines. *Id.* ¶ 3. Defendant HCM is a Maine corporation which operated a nursing home at a site in Belfast, Maine, owned by Tall Pines. *Id.* ¶ 6. Defendant Larry M. Brown was at one time the sole shareholder in HCM and one of two general partners in Tall Pines. *Id.* ¶ 8. Defendants Shelter Group, Inc. and PropSys are Maine corporations which directly or indirectly controlled TPM and Tall Pines. *Id.* ¶¶ 4-5. Defendants Stephen L. Griswold and Terence E. Nadeau are Maine residents who directly or indirectly controlled Tall Pines, TPM, Shelter Group, PropSys, and HCM. *Id.* ¶ 7.

Tall Pines owned and leased real estate known as Tall Pines Manor, which was operated by HCM as a 70-bed nursing home. *Id.* ¶ 16. Some time before January 12, 1995, the defendants formulated a plan to buy out the interests of the limited partners of Tall Pines. *Id.* ¶ 19. Refinancing of the mortgage debt of Tall Pines was part of this plan. *Id.* ¶ 20. The plan provided for the purchase of all of the assets of Tall Pines for less than their fair market value and for liquidation of the limited partnership. *Id.* ¶ 22. On January 12, 1995, defendant Nadeau sent a letter on defendant PropSys's

stationery, stating that he was writing on behalf of defendant TPM, to all limited partners of Tall Pines. *Id.* ¶ 23 & Exh. C. The letter stated, *inter alia*, that TPM had received an offer from HCM to purchase all of the tangible assets and liabilities of Tall Pines for $3,015,000; that the fair market value of those assets was less than the offer; that TPM based its analysis of the value of those assets upon the opinion of an appraiser; that each limited partnership share would receive approximately $34,460 in proceeds from the proposed sale; and that Nadeau and defendant Griswold were negotiating with defendant Brown to "re-associate our ownership interests in . . . Health Care [Management]." *Id.* ¶ 25-26 & Exh. C at 6. Some limited partners were offered additional money as an inducement to agree to the sale. *Id.* ¶ 29.

A majority of the limited partners, including some of the plaintiffs, signed the Consent and Release to the sale which accompanied the Nadeau letter. *Id.* ¶ 30. The sale was completed on or about January 25, 1995, and each limited partner, except plaintiff Morin, received $34,500. *Id.* ¶ 31. The Nadeau letter contained false and misleading statements. *Id.* ¶ 32. The defendants also concealed and misrepresented other facts material to the sale. *Id.* ¶ 33. The distribution of the sale proceeds failed to comply with the Partnership Agreement. *Id.* ¶ 34.

The second amended complaint presents the following claims: Count I asserts securities violations under 15 U.S.C. § 78j and Securities and Exchange Commission ("SEC") Rule 10b-5 against all defendants; Count II asserts securities violations under 32 M.R.S.A. § 10201(2) against all defendants; Count III asserts securities violations under 32 M.R.S.A. § 10201(1) against all defendants; Count IV asserts breach of fiduciary duty against all defendants except HCM; Count V asserts common-law fraud against all defendants; Count VI asserts breach of a third-party beneficiary contract against defendants TPM, Griswold and Nadeau; Count VII asserts breach of the partnership

agreement against all defendants except HCM ; Count VIII asserts negligent misrepresentation against all defendants except HCM; Count IX asserts conversion against all defendants; Count X seeks a partnership accounting under Maine statutes from defendant TPM; Count XI asserts the RICO claim against defendants Griswold, Nadeau, Shelter Group and PropSys; Count XII asserts diversion of a partnership opportunity against defendants Brown, TPM, Griswold and Nadeau; and Count XIII asserts a common-law conspiracy to defraud against all defendants.

C. Defendant HCM's Motion to Dismiss

1. The securities claims.

HCM seeks dismissal of all claims against it (Counts I, II, III, V, VIII, IX, and XIII) for failure to state a claim upon which relief may be granted. HCM first addresses the securities fraud claims set forth in Counts I, II, and III. The parties agree that 32 M.R.S.A. § 10201 is the analogue to 15 U.S.C. § 78j and Rule 10b-5 of the SEC, and thus that analysis of Counts II and III, asserted under the state statute, is subject to the same framework as Count I, which is based on the federal law. *See Dyer v. Eastern Trust & Banking Co.*, 336 F. Supp. 890, 906 (D. Me. 1971) (predecessor statute to 32 M.R.S.A. § 10201 is analogue to § 10(b) of the Securities and Exchange Act and Rule 10b-5).

HCM argues that the sale of the assets of Tall Pines, rather than the limited partnership shares, was not a sale of securities under relevant law. The plaintiffs respond that the sale of all of the assets of a limited partnership and the distribution of proceeds to the owners, which the complaint alleges is what happened here, is a "forced sale" of a security under federal law, relying on *Mayer v. Oil Field Sys. Corp.*, 721 F.2d 59, 63 (2d Cir. 1983), and *Alley v. Miramon*, 614 F.2d

1372, 1384-85 (5th Cir. 1980). Neither case is sufficiently similar on its facts to be dispositive of this issue in the instant case. The available case law on the specific question is divided. Limited partners in such circumstances were allowed to bring suit under 15 U.S.C. § 78j in *Engl v. Berg*, 511 F. Supp. 1146, 1152, 1339 (E.D. Pa. 1981) and *Houlihan v. Anderson-Stokes, Inc.*, 434 F. Supp. 1330, 1339 (D. D.C. 1977). In *Fershtman v. Schectman*, 450 F.2d 1357 (2d Cir. 1971), the plaintiff limited partners were not allowed to assert such a claim, primarily due to the terms of the partnership agreement. *Id*. at 1360. The partnership agreement is not part of the record in this case, so *Fershtman* is of limited value in resolving this issue.

Fairly close on its facts is *Natowitz v. Mehlman*, 567 F. Supp. 942 (S.D.N.Y. 1983), in which a limited partner sued the general partner and others after the sale of the partnership's sole asset. The court rejected the securities fraud claim, based on the "forced sale" doctrine, because the alleged fraudulent conduct did not "touch" the securities transaction, as required by *Superintendent of Ins. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 12-13 (1971).

> Although [the plaintiff's] amended complaint clearly alleges that defendants had an intent to defraud the partnership of its sole asset, and although the alleged forced sale was necessarily a direct consequence of such fraud, it cannot be said that the forced sale was an integral or even helpful part of the fraud. Simply stated, the alleged forced sale resulted not from fraud in connection with the purchase or sale of securities but from fraud in connection with the sale of the partnership's assets.

Natowitz, 567 F. Supp. at 947. *See also Batchelder v. Northern Fire Lites, Inc.*, 630 F. Supp. 1115, 1120 (D.N.H. 1986) (no forced sale when corporation's major asset sold but corporation continued to exist and plaintiff held shares); *Arnesen v. Shawmut County Bank, N.A.*, 504 F. Supp. 1077, 1082 (D. Mass. 1980) (where corporation continues to exist, albeit without assets, and plaintiffs continue to own shares, no forced sale for purposes of a section 78j claim).

The plaintiffs suggest that it is "questionable whether the reasoning of these cases is valid," Plaintiffs' Opposition to Motion to Dismiss of TPM (Docket No. 19) at [3], relying on the contrary position expressed by the *Engl* and *Houlihan* courts. More substantively, the plaintiffs attempt to distinguish these cases because the Tall Pines limited partners also agreed to dissolve and liquidate the partnership when they agreed to the sale, although that has not yet occurred. Second Amended Complaint, Exh. D at 1. That distinction, however, does not bring the Tall Pines sale outside the holdings of *Natowicz, Batchelder* and *Arnesen.*

Those holdings are reinforced by the Supreme Court's decision in *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083 (1991), in which minority shareholders brought an action alleging securities fraud in the proxy statement issued in connection with a majority shareholder's "freeze out" of the minority shares in a merger. The Court held that the plaintiffs could not show damage causation when their votes were not necessary to authorize the corporate action, and that, therefore, they had no cause of action under the Securities and Exchange Act. 501 U.S. at 1108. The plaintiffs attempt to distinguish *Virginia Bankshares* by arguing that the defendants here never owned or controlled a majority interest in Tall Pines. That factual allegation is not present in the second amended complaint and therefore cannot provided the basis for a ruling on the motion to dismiss. In any event, the issue under *Virginia Bankshares* does not appear to be whether the persons whom the dissenting shareholder chooses to name as defendants controlled a majority interest in the corporation, but whether the votes of the plaintiffs were necessary to authorize the action of which they complain. The plaintiffs have made no such showing here.

Applying *Viriginia Bankshares* by analogy, and finding the cases rejecting the "forced sale" doctrine more persuasive, I find that dismissal of the securities fraud claims, Counts I-III of the

second amended complaint, is appropriate. It is therefore not necessary to address HCM's additional argument that the second amended complaint fails to comply with the requirements of Fed. R. Civ. P. 9(b), that fraud be pleaded with particularity, and Fed. R. Civ. P. 23.1, which applies to derivative actions.

2. The state law fraud claim

HCM's motion to dismiss the common-law fraud claim set forth in Count V of the second amended complaint is based on the same argument it raised in the alternative against the securities fraud claims: that the plaintiffs have failed to allege any misleading communication by HCM to the plaintiffs. The allegation that misrepresentations in the Solicitation Letter were made on behalf of HCM, Second Amended Complaint ¶¶ 24 & 32, is sufficient to withstand a motion to dismiss for purposes of the securities law claims. *See Ouaknine v. MacFarlane*, 897 F.2d 75, 78 (2d Cir. 1990) (offering memorandum signed by one defendant "on behalf of" four other defendants satisfies Rule 9(b) particularity requirements). It is sufficient for this claim as well.

3. The negligent misrepresentation claim

HCM asserts, without citation to authority, that the plaintiffs have failed to allege a cause of action against it for negligent misrepresentation (Count VIII). The plaintiffs respond that the second amended complaint does not seek recovery against HCM on this count. Plaintiffs' Opposition to HCM's Motion to Dismiss (Docket No. 14) at 9. This is not at all clear from Count VIII itself, which demands judgment "against the Defendants" in general. In order to make the record clear, I recommend that HCM's motion to dismiss be granted as to Count VIII of the second amended complaint.

4. The conversion claim

As for the conversion claim (Count IX), HCM seeks dismissal because the plaintiffs have failed to allege that HCM wrongfully exerted control over the property at issue and that any demand was made upon HCM for return of the property. Under Maine law, "the gist of conversion is an invasion of a party's possession or right to possession." *Doughty v. Sullivan*, 661 A.2d 1112, 1122 (Me. 1995). In addition to establishing invasion of possession, a plaintiff must also show

> (1) a property interest in the goods; (2) the right to their possession at the time of the alleged conversion; and (3) when the holder has acquired possession rightfully, a demand by the person entitled to possession and a refusal by the holder to surrender.

Chiapetta v. LeBlond, 505 A.2d 783, 785 (Me. 1986). Assuming without deciding that conversion may be asserted as a derivative claim, as the second amended complaint purports to do at paragraph 61, or that the plaintiffs as owners of limited partnership shares were entitled to possession of some or all of the assets of Tall Pines, as claimed in paragraph 63,[1] the second amended complaint fails to allege that the plaintiffs have demanded a return of any assets by HCM. More important, the second amended complaint by its own terms shows that the plaintiffs did not have any right to possession at the time of the transfer, because a majority of the partners approved the sale. Amended Complaint ¶¶ 30-31. Count IX should be dismissed.

5. The conspiracy claim

The final count as to which relief is sought against HCM is for common law conspiracy. HCM argues that this count contains "nothing more than . . . conclusory allegations of . . . conspiracy

[1] These two claims, both included in Count IX, appear to be inconsistent. Either the plaintiffs are asserting a derivative claim on behalf of Tall Pines or they are asserting their own right to possession. However, the court need not resolve this apparent contradiction in the circumstances here.

against HCM without sufficient factual allegations." HCM's Objection to Plaintiffs' Second Motion to Amend Complaint (Docket No. 23) at 2. Under Maine common law, "conspiracy is not a separate tort but rather a rule of vicarious liability." *McNally v. Mokarzel*, 386 A.2d 744, 748 (Me. 1978). Dismissal of this count is therefore appropriate. *Id.*

D. The Motion for Judgment on the Pleadings

Defendants Griswold, Nadeau, Shelter Group and TPM move for judgment on the pleadings as to all counts asserted against them. For the reasons stated above, they are entitled to judgment on the pleadings on the securities fraud claims, Counts I - III of the second amended complaint.

These defendants next address the only remaining claim under federal law, Count XI, which alleges violation of 18 U.S.C. § 1961 *et seq.* (RICO). A plaintiff may not "rely upon any conduct that would have been actionable as fraud in the purchase or sale of securities to establish a violation of section 1962." 18 U.S.C. § 1964(c). The second amended complaint lists six "predicate acts" involving the use of the mail, in addition to incorporating the earlier allegations of fraud. Second Amended Complaint ¶¶ 66-67. The defendants argue that the plaintiffs have failed to allege facts constituting a pattern of racketeering activity. All parties to this motion rely on *Roeder v. Alpha Indus., Inc*., 814 F.2d 22 (1st Cir.1987).

Rule 9(b) applies to civil RICO actions. *Cutler v. FDIC*, 781 F. Supp. 816, 818 (D. Me. 1992). Thus, the allegations of non-securities fraud in the second amended complaint must be pleaded with particularity. The complaint must specify the time, place and content of an alleged false representation, but not the circumstances from which fraudulent intent could be inferred. *Id*. Paragraph 67 of the second amended complaint satisfies this standard.

In order to allege a pattern of racketeering activity under RICO, at least two acts of racketeering activity must be set forth. *Roeder*, 814 F.2d at 30. "The constituent elements must be sufficiently related to one another and threaten to be more than an isolated occurrence." *Id.* The second amended complaint appears to present a relationship among the alleged acts that is sufficient for purposes of surviving a motion testing the sufficiency of the complaint. The issue of continuity is a closer question, however.

> In order to establish the continuity of the predicate acts, a plaintiff must show either 1) that the acts amount to continued criminal activity, in that the related acts extend over a period of time; or 2) that the predicate acts, though not continuous, pose a threat of continued activity.

Libertad v. Welch, 53 F.3d 428, 445 (1st Cir. 1995). The second amended complaint does not demonstrate "a realistic prospect of continuity over an open-ended period yet to come," *id*. (citation omitted), the definition of the second alternative. Therefore, the allegations must establish a closed-end period of continued criminal conduct over a period of more than a few months. *Id.* The allegations in paragraph 67, while not specific as to actual dates, allege predicate acts from 1990 through 1995. This is a sufficient period to meet the requirements of the first continuity alternative.

On the grounds asserted by the defendants, I conclude that the motion for judgment on the pleadings as to Count XI should be denied. The motion for judgment on the pleadings does not address the state-law claims directly, merely asking that the court dismiss them pursuant to 28 U.S.C. § 1367(c) in the event that the federal-law counts are all dismissed. If the court adopts my recommendation that Count XI not be dismissed, this request is rendered moot.

IV. Conclusion

For the foregoing reasons, the plaintiffs' motions to amend the complaint are **GRANTED**. In this regard, the plaintiffs shall forthwith serve Larry M. Brown with the second amended complaint. Further, I recommend that defendant HCM's motion to dismiss be **GRANTED** as to Counts I-III, VIII, IX and XIII of the second amended complaint and otherwise **DENIED**; and that the motion for judgment on the pleadings of defendants TPM, Shelter Group, Griswold, and Nadeau be **GRANTED** as to Counts I-III of the second amended complaint and otherwise **DENIED**.

NOTICE

A party may file objections to those specified portions of a magistrate judge's report or proposed findings or recommended decisions entered pursuant to 28 U.S.C. § 636(b)(1)(B) for which de novo review by the district court is sought, together with a supporting memorandum, within ten (10) days after being served with a copy thereof. A responsive memorandum shall be filed within ten (10) days after the filing of the objection.

Failure to file a timely objection shall constitute a waiver of the right to de novo review by the district court and to appeal the district court's order.

Dated at Portland, Maine this 5th day of June, 1997.

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David M. Cohen
United States Magistrate Judge